No. 26

In the Supreme Court of the United States

October Term, 1956

Max Putnam and Elizabeth Putnam, Petitioners

v.

Commissioner of Internal Revenue

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE [illegible] CIRCUIT

BRIEF FOR THE RESPONDENT

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OCTOBER TERM, 1956

No. 25

MAX PUTNAM AND ELIZABETH PUTNAM, PETITIONERS

v.

COMMISSIONER OF INTERNAL REVENUE

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE EIGHTH CIRCUIT

BRIEF FOR THE RESPONDENT

OPINIONS BELOW

The findings of fact and opinion of the Tax Court (R. 14-21) are not officially reported. The opinion of the Court of Appeals (R. 27-34) is reported at 224 F. 2d 947.

JURISDICTION

The judgment of the Court of Appeals was entered on August 11, 1955. (R. 35.) By order of Mr. Justice Clark, dated November 9, 1955, the time for filing a petition for a writ of certiorari was extended to and including January 7, 1956. The petition for a writ of certiorari, filed on January 5, 1956, was granted on February 27, 1956. (R. 36.) 350 U. S. 964. The

jurisdiction of this Court rests upon 28 U. S. C., Section 1254.

QUESTION PRESENTED

Taxpayer, the controlling stockholder of a corporation, guaranteed payment of promissory notes which the corporation executed in obtaining bank loans. The corporation having become insolvent, taxpayer as guarantor was required to pay the bank, and the corporation was unable to repay him.

The question presented is whether, as taxpayer contends, the amount paid by the taxpayer to the bank was a nonbusiness loss (not involving a bad debt) deductible in full under Section 23 (e) (2) of the Internal Revenue Code of 1939; or whether, as both courts below held, upon his payment as guarantor the taxpayer by subrogation acquired a debt, the loss resulting from the worthlessness of which is deductible only as a capital loss under Section 23 (k) (4).

STATUTES AND REGULATIONS INVOLVED

Pertinent provisions of Sections 23 (e), (g), (k) and 117 (d) of the Internal Revenue Code of 1939, and of Sections 29.23 (e)-1, 29.23 (g)-1 and 29.23 (k)-6 of Treasury Regulations 111 appear in the Appendix, *infra*, pp. 31-36.

STATEMENT [1]

The taxpayers, Max and Elizabeth Putnam, are husband and wife who filed a joint income tax return

[1] Only the facts relating to the single issue presented by the petition for certiorari are summarized. See footnote 2, p. 10, *infra*.

for the taxable year 1948. Max Putnam, hereinafter called taxpayer, is a lawyer who since 1931 has been continuously engaged in the general practice of law in Des Moines.

In 1946 taxpayer, with Meredith Case and Leo Quinn, formed a corporation, the Whitehouse Publishing Company, for the purpose of carrying on a general printing and publishing business. (R. 14–15.) The authorized capital stock of the corporation consisted of 15 shares having a par value of $100 a share. Each of the organizers—taxpayer, Case, and Quinn—received 5 shares of the stock. The corporation's capital was contributed by taxpayer on behalf of himself and the other two organizers, who gave him their notes for his contributions on their behalf and pledged their shares as security. In 1947 Case and Quinn defaulted in payment of their notes, and their shares were transferred to taxpayer. (R. 15–16.)

Taxpayer personally guaranteed payment for all supplies purchased by Whitehouse and payment of the salaries of its employees. In August 1946, taxpayer and Whitehouse borrowed $12,075 from a bank for use of the corporation, and in March 1947 borrowed an additional $5,000 from the bank for use of the corporation. Taxpayer and Whitehouse signed promissory notes for the amounts for that purpose, as co-makers. In November 1946, taxpayer borrowed $3,500 and made it available to the corporation. (R. 16.)

By the middle of 1947, it was evident that the publishing venture was unsuccessful. In July 1947,

Whitehouse was receiving some income from payments on purchase orders for a publication it had printed, but its only substantial assets were in its building and equipment. At the same time, it had an indebtedness of $13,500. During that month, Whitehouse ceased doing business and sold its building for $7,000. Of this amount, $5,000 was applied to the unpaid balance of the promissory note of August, 1946, and $2,000 went to taxpayer to pay him for his advances to the corporation. In December 1948, taxpayer paid to the bank the remaining $3,500 due on the promissory note of August, 1946, and the $5,000 due on the promissory note of March 1947. (R. 16–17.)

In ~~his 1948~~ income tax return, filed jointly with his wife, taxpayer claimed a business bad debt deduction in the amount of $9,005.21, which consisted of the $8,500 paid to the bank on the promissory notes executed by taxpayer and the corporation as co-makers, together with interest on those notes. The Commissioner of Internal Revenue determined, however, that the amount due the taxpayer from the corporation by reason of his payments of the notes represented nonbusiness bad debts, and that therefore the taxpayer's losses were deductible only as short-term capital losses under Section 23 (k) (4) of the Internal Revenue Code of 1939. (R. 9, 17.)

Taxpayer filed a petition for redetermination in the Tax Court, contending that he had really acted only as guarantor and not as co-maker of the notes, and that his payments on those notes resulted in business bad debts deductible in full under Section 23 (k) (1) of

the Internal Revenue Code of 1939. In the alternative, taxpayer contended, *inter alia,* that, if his payments as guarantor did not result in business bad debts, the amount of such payments was deductible in full under Section 23 (e) (2) as a loss incurred in a transaction entered into for profit although not connected with a trade or business. (R. 17–18.)

Although accepting the taxpayer's contention, and finding as a fact, that his payments to the bank were made as guarantor, the Tax Court concluded that the payments resulted in nonbusiness bad debts and that therefore the taxpayer's losses were deductible only as short-term capital losses under Section 23 (k) (4). Accordingly, decision was entered in favor of the Commissioner. The Court of Appeals unanimously affirmed. (R. 19–21, 35.)

SUMMARY OF ARGUMENT

Section 23 (e) (2) of the Internal Revenue Code of 1939 authorizes the deduction in full of an individual's nonbusiness losses, if incurred in a transaction entered into for profit. However, Section 23 (k) (4), added to the Code in 1942, removes from the operation of that section a particular class of nonbusiness losses—nonbusiness bad debt losses—and requires that they be treated as capital losses. Consequently, in order for a nonbusiness loss to qualify for deduction in full, it is not enough for the taxpayer to bring himself within the general provisions of Section 23 (e) (2); he must also show that the loss falls outside the spe-

cial capital loss limitation provisions of Section 23 (k) (4)—*i. e.*, that it was not a bad debt loss. By according capital loss treatment to nonbusiness bad debt losses, Section 23 (k) (4) places such losses on a tax parity with similar nonbusiness losses resulting from the worthlessness of investments evidenced by debt or stock securities. Section 23 (g) (2) and (3), and (k) (2) and (3).

The court below properly approved the Commissioner's and the Tax Court's determination that the loss here in question was deductible as a nonbusiness bad debt loss under the special provisions of Section 23 (k) (4), and consequently as a capital loss, not as an ordinary loss under the general provisions of Section 23 (e) (2). The loss resulted from taxpayer's payment as guarantor of a bank loan made to a corporation of which he was organizer and dominant stockholder, and from the corporation's inability to repay him. That the loss was of a nonbusiness character is no longer in issue. That it constituted a bad debt loss within the purview of Section 23 (k) (4) is apparent from (1) the nature of a guarantor's loss, (2) the administrative and judicial treatment of guarantors' losses under the statutory provisions preceding those here involved, and (3) the subsequent legislation with respect to both bad debt losses generally and guarantors' bad debt losses in particular.

It is well settled both generally and under Iowa law that a guarantor upon being required to make payment under his guaranty contract acquires the rights of the creditor by subrogation. The law implies a promise on the part of the principal debtor to reim-

burse the guarantor, and the guarantor's payment is treated not as extinguishing the debt but as merely substituting the guarantor for the creditor. While a guarantor by entering into the guaranty contract and making payment thereunder puts himself in a position where he may sustain a loss, it is only if (and to the extent that) the debt which he acquires by subrogation becomes worthless that he actually sustains a loss. Thus, if he is able to recover in full from the principal debtor, he clearly suffers no loss at all. Since the existence and extent of the loss is wholly and directly dependent upon the worthlessness of the debt owing by the principal debtor, the loss if it occurs is necessarily attributable to the worthlessness of that debt and must therefore be considered a bad debt loss. And since the corporation whose debt taxpayer guaranteed was still in existence, although insolvent, when he made the guaranty payment, the courts below correctly held that upon such payment taxpayer acquired a debt by subrogation, the loss from the worthlessness of which must be considered a capital loss under Section 23 (k) (4).

Both the administrative and the judicial construction of the bad debt provisions of earlier revenue laws recognized that those provisions covered guarantors' losses. With this long-standing construction in the background Congress repeatedly reenacted those provisions without substantial change and without expressing any disagreement with such construction. Under familiar principles, Congress is presumed to have accepted this construction as a correct interpretation of the statute; at all events, there is

no indication that Congress meant to depart from such construction when it enacted the bad debt provisions applicable here. Accordingly, those provisions should be construed to include an individual's non-business losses as guarantor. Congress has also adhered to its consistent treatment of guarantors' losses as bad debt losses in subsequent legislation dealing specifically with certain losses of guarantors of non-corporate obligations.

Furthermore, under taxpayer's construction of the statute, the extent of deductibility of losses from investments in an unsuccessful corporate venture would become dependent entirely on the form rather than the substance of the transaction. Had taxpayer invested the amount involved in exchange for additional stock, his loss upon failure of the corporation unquestionably would have been a capital loss. Section 23 (g) (2) and (3). Had he made the investment by way of a direct loan evidenced by a debt security of the corporation, his loss would likewise have represented a capital loss. Section 23 (k) (2) and (3). And had he made the investment by way of a simple ordinary loan to the corporation, his loss would also have constituted a capital loss. Section 23 (k) (4).

Nothing in the scheme or language of the statute or its history warrants the assumption that Congress intended to accord preferential tax treatment to a loan or an investment loss merely because the transaction takes the form of a guaranty of a loan made by a third party to the corporation. The situation here is essentially the same, legally and practically, as if

taxpayer had borrowed the money from the bank and then lent it to the corporation. In both cases his loss arises from the failure of the corporation to repay him. In both cases the insolvency of the corporation is relevant in determining *when* the loss occurred, not the nature of the loss. In the one case, as in the other, the loss is deductible as a capital loss under Section 23 (k), not as an ordinary loss under Section 23 (e).

ARGUMENT

TAXPAYER'S NONBUSINESS LOSS AS GUARANTOR WAS A BAD DEBT LOSS SUBJECT TO THE LIMITATIONS ON DEDUCTIBILITY CONTAINED IN SECTION 23 (K) (4) OF THE INTERNAL REVENUE CODE OF 1939

A. *Introductory*

The taxpayer, organizer and controlling stockholder of a corporation, financed its activities by making capital contributions, by making direct loans, and by procuring a bank loan which he individually guaranteed. The corporate venture having proved unsuccessful, taxpayer was obliged as guarantor to pay the bank loan, and was unable to obtain repayment from the corporation. The immediate question presented is whether taxpayer's loss resulted from his payment as guarantor of the corporation's unpaid debt and is deductible in full as an ordinary nonbusiness loss under Section 23 (e) (2) of the Internal Revenue Code of 1939 (Appendix, *infra*, p. 31), as taxpayer contends, or was a nonbusiness bad debt deductible only as a capital loss under Section 23 (k)

(4) (Appendix, *infra*, p. 33), as both courts below held.[2] Upon the determination of that issue hinges the answer to the broader, underlying question, namely, whether an investor in an unsuccessful corporate venture is entitled to a greater loss deduction for tax purposes if he guarantees loans by third parties to the corporation than if he invests his money directly, e. g., by lending money to the corporation or by buying its stock.

The nonbusiness loss suffered by an individual who has lent money to an unsuccessful corporation is treated as a capital loss.[3] The same treatment is given to the nonbusiness loss of an individual who has provided capital for a corporation in the conventional

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[2] Taxpayer alternatively contended below that the loss in question was deductible in full under Section 23 (k) (1) (Appendix, *infra*, p. 32) as a business bad debt, or under Section 23 (e) (1) (Appendix, *infra*, p. 31) as a business loss other than one resulting from a bad debt. Both courts below found that the loss was of a nonbusiness rather than of a business character, and taxpayer does not challenge their concurrent findings on that issue. The only question raised by his petition for certiorari, and accordingly the only issue here presented (*Helvering* v. *Taylor*, 293 U. S. 507, 511), is whether the loss is deductible under Section 23 (k) (4) as a nonbusiness bad debt loss, or under Section 23 (e) (2) as a nonbusiness loss other than a bad debt loss.

[3] Under Section 23 (k) of the Internal Revenue Code of 1939 (Appendix, *infra*, pp. 32-33), the treatment of such a loss as one from the sale or exchange of a capital asset may be required under either paragraph (2) or paragraph (4), depending upon whether or not the loan is evidenced by a security as defined in paragraph (3). Similar provisions are contained in Sections 165 (g) and 166 (d) and (e) of the Internal Revenue Code of 1954 (26 U. S. C. 1952 ed., Supp. II, Secs. 165 and 166).

form of purchasing its stock.[4] The general effect of such treatment is to restrict an individual's nonbusiness loss deductions, since his losses from sales or exchanges of capital assets are deductible only to the extent of his gains from such sales or exchanges, plus his net income or $1,000, whichever is smaller.[5]

Taxpayer contends that the amount which he as guarantor was required to pay the lending bank on the promissory notes of his then wholly owned and insolvent corporation is fully deductible under Section 23 (e) (2) as a nonbusiness loss other than a bad debt loss. The corollary of this contention is that because he made the necessary operating funds available to the corporation indirectly, by lending his credit—*i. e.,* by guaranteeing payment of the bank's loans to the corporation—he is entitled to a greater loss deduction than he would have been entitled to if he had supplied those necessary funds directly. Yet, as a practical matter, taxpayer's loss would have been precisely the same if he had borrowed the money from the bank himself and then lent it to the corporation.

It is the Commissioner's position that the loss incurred by taxpayer as guarantor of loans to his corporation constituted a nonbusiness bad debt loss falling within the purview of Section 23 (k) (4),

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[4] See Section 23 (g) (2) and (3), Internal Revenue Code of 1939 (Appendix, *infra,* pp. 31–32), and Section 165 (g), Internal Revenue Code of 1954, *supra.*

[5] See Section 117 (d), Internal Revenue Code of 1939 (Appendix, *infra,* p. 33), and Section 1211, Internal Revenue Code of 1954 (26 U. S. C. 1952 ed., Supp. II, Sec. 1211).

and consequently is no less subject to the capital loss limitations imposed by that section than losses resulting from direct loans to the corporation. To hold that taxpayer is entitled to a greater loss deduction merely because he lent his credit to the corporation, rather than his money in the first instance, would exalt form over substance and make the tax result depend upon a distinction having no relation to the business realities of such transactions. Nothing in the relevant statutory provisions or their history justifies the conclusion that Congress intended to create any such distinction; and the court below, agreeing with the Tax Court and the well-reasoned dissenting opinion of Judge Stewart in *Cudlip* v. *Commissioner*, 220 F. 2d 565 (C. A. 6th), properly refused to draw one.

B. *Nonbusiness bad debt losses are deductible as capital losses under Section 23 (k) (4), not as ordinary losses under Section 23 (e) (2)*

Section 23 (k) (4) of the Internal Revenue Code of 1939 provides:

> *Non-business debts.*—In the case of a taxpayer, other than a corporation, if a non-business debt becomes worthless within the taxable year, the loss resulting therefrom shall be considered a loss from the sale or exchange, during the taxable year, of a capital asset held for not more than 6 months. The term "non-business debt" means a debt other than a debt evidenced by a security as defined in paragraph (3) and

> other than a debt the loss from the worthlessness of which is incurred in the taxpayer's trade or business.

These provisions were added to the Code by Section 124 (a) of the Revenue Act of 1942, c. 619, 56 Stat. 798. Their purpose, as stated in the House Ways and Means Committee Report accompanying the 1942 Revenue Bill, was "to remove existing inequities and to improve the procedure through which bad-debt deductions are taken." H. Rep. No. 2333, 77th Cong., 2d Sess., p. 44 (1942-2 Cum. Bull. 372, 408). Their effect is to subject nonbusiness bad debt losses, which might otherwise qualify for deduction in full under Section 23 (e) (2), to the limitations upon capital losses, and thus place them on a tax parity with similar nonbusiness losses which are accorded capital loss treatment.

Prior to the Revenue Act of 1942, in computing an individual's taxable net income, nonbusiness bad debts received more favorable tax treatment than was generally afforded other nonbusiness losses. Thus, an individual's bad debts, whether business or nonbusiness, were deductible in full.[6] On the other hand, only some of an individual's nonbusiness losses (other than casualty or theft losses) were deductible, *viz.*, those incurred in transactions entered into for profit.[7] Moreover, not all deductible losses were fully deductible. A bad debt loss was deductible only as a

[6] See Section 23 (k) (1), Internal Revenue Code of 1939 (26 U. S. C. 1940 ed., Sec. 23).

[7] See Section 23 (e), Internal Revenue Code of 1939 (Appendix, *infra*, p. 31).

capital loss if the debt was evidenced by a corporate security, and like treatment was accorded worthless stock losses and losses from sales or exchanges of capital assets.[8]

The Revenue Act of 1942, by restricting the deduction of nonbusiness bad debts, brought the tax treatment of those items into closer conformity with that generally afforded an individual's nonbusiness losses.[9] This was accomplished by the amendment of paragraph (1) of Section 23 (k), and the addition of paragraph (4) to that section. Paragraph (1) was amended to provide that it "shall not apply * * * with respect to a nonbusiness debt" as defined in paragraph (4), and the latter paragraph was added to provide that the "loss" resulting from the worthlessness [10] of a nonbusiness debt was to be considered

[8] See paragraphs (1), (2) and (3) of Section 23 (g), and paragraphs (2) and (3) of Section 23 (k), Internal Revenue Code of 1939 (Appendix, *infra*, pp. 31–32).

[9] At the same time, by the addition of a new subsection (a) (2) to Section 23 of the Internal Revenue Code of 1939 by Section 121 (a) of the Revenue Act of 1942, an individual was authorized to deduct nonbusiness expenses paid or incurred in certain profit transactions.

[10] The Revenue Act of 1942, *supra*, also made the test of deductibility, in the case of bad debts and certain worthless securities evidencing indebtedness, similar to that applied in the case of certain worthless securities evidencing ownership. Prior to that Act, a deduction was authorized if certain securities evidencing ownership became worthless during the taxable year. See Section 23 (g) (2) and (3), Internal Revenue Code of 1939 (26 U. S. C. 1940 ed., Sec. 23 (g)). At the same time, deductions were authorized in the case of bad debts and certain worthless securities evidencing indebtedness only if such debts or securities were ascertained to be worthless and charged off within the taxable year. See Section 23 (k) (1), (2) and (3),

a loss from the sale or exchange of a capital asset. By limiting the bad debts which an individual might deduct as such to business bad-debts, and by requiring nonbusiness bad debts to be treated as capital losses, Congress in effect carved out of the general category of losses a particular class of losses, namely, nonbusiness bad debt losses, and expressly subjected them to capital loss limitations—just as it had previously done (in Section 23 (g) (2) and (3) and (k) (2) and (3)) with respect to debt and stock interests evidenced by securities. It is thus clear from the statutory pattern which emerged from the 1942 amendments that, irrespective of whether a nonbusiness bad debt loss might otherwise qualify for deduction in full under the general provisions of Section 23 (e) (2), *i. e.*, as a nonbusiness loss incurred in a transaction entered into for profit,[11] such a loss is deductible only as a capital loss by virtue of the special limitation provisions contained in Section 23 (k) (4).

Internal Revenue Code of 1939 (26 U. S. C.—1940 ed., Sec. 23 (k)). Upon adoption of the Revenue Act of 1942, the test in each case became whether the debt or security became worthless during the taxable year, the ascertainment of worthlessness and charge-off requirement (with an exception not relevant here) being eliminated.

[11] The determination whether a loss is a business or nonbusiness loss being substantially the same as the determination whether a debt is a business or nonbusiness debt (H. Rep. No. 2333, 77th Cong., 2d Sess., pp. 77–78 (1942–2 Cum. Bull. 372, 431); Section 29.23 (k)–6, Treasury Regulations 111), a nonbusiness bad debt loss cannot, of course, be deducted as a business loss under Section 23 (e) (1). Nor, since a bad debt loss is obviously not a casualty or theft loss, can it be deducted under Section 23 (e) (3).

In *Spring City Co.* v. *Commissioner,* 292 U. S. 182, involving the pre-1942 statutory provisions, this Court, in disallowing a bad debt deduction claimed under the general loss provision, stated (p. 189), that "The making of the specific provision as to debts indicates that these were to be considered as a special class and that losses on debts were not to be regarded as falling under the preceding general provision." Similarly, the special capital loss provision of Section 23 (k) (4) added by the 1942 Act and dealing specifically with nonbusiness bad debt losses, rather than the general loss provision of Section 23 (e) (2), governs the extent of the deductibility of a nonbusiness bad debt loss.

Taxpayer erroneously assumes (Br. 6–7) that Section 23 (k) (4) was aimed merely at family and friendship transactions which purported to create debts but were actually gifts. No new legislation was needed to accomplish that purpose, for such transactions do not give rise to deductible debts at all. On the contrary, as is plain from the language of the section, it was intended to apply comprehensively to all "non-business" bad debt losses, irrespective of whether the lender or borrower (or guarantor) is an individual or a corporation or of whether they are related or unrelated by ties of family or friendship. Nor is there any warrant for taxpayer's further assumption (Br. 7–11) that Section 23 (k) (4) was not intended to apply to non-business bad debts arising by operation of law. Of course, not every obligation

necessarily represents an indebtedness.[12] But Section 23 (k) (4) by its very terms applies to any "nonbusiness debt", however it arises. (And see pp. 19–21, *infra.*)

Accordingly, even assuming as taxpayer contends (Br. 17–18) that he entered into a transaction for profit when he guaranteed repayment of the loans to his corporation, the loss resulting from the guaranty transaction is nonetheless subject to the capital loss limitations imposed by the special provisions of Section 23 (k) (4) if it represented a nonbusiness bad debt loss. Since there is no question that the loss was of a nonbusiness character (see n. 2, *supra,* p. 10), the narrow question which remains—and upon which this case turns—is whether the loss was, as both courts below held, a bad debt loss. If it was, then Section 23 (k) (4) applies and taxpayer is entitled only to a capital loss deduction.

C. *The loss in question was a bad debt loss*

The courts below correctly concluded that taxpayer's nonbusiness loss as guarantor was a bad debt loss subject to the capital loss limitations on deductibility contained in Section 23 (k) (4) of the Internal Revenue Code of 1939, *supra.* The correctness of their conclusion becomes apparent upon examination of (1) the nature of a guarantor's loss, (2) the tax treatment afforded such a loss long prior to the enact-

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[12] Thus, *Hanes* v. *Commissioner*, 2 T. C. 213, to which taxpayer points (Br. 7–8) as allegedly illustrating an inconsistency in the Commissioner's position, did not involve a debt but merely an unadjudicated damage claim for fraud.

ment of Section 23 (k) (4), and (3) the subsequent legislation with respect to both bad debt losses generally and guarantors' bad debt losses in particular.

The principle is well established, both generally and in the State of Iowa,[13] that a guarantor who is required to make payment under his guaranty contract succeeds to the rights of the creditor by subrogation. The law implies a promise on the part of the principal debtor to reimburse the guarantor, and the guarantor's payment is treated not as extinguishing the debt but as merely substituting the guarantor for the creditor. *Aetna Life Ins. Co.* v. *Middleport,* 124 U. S. 534, 548; *United States* v. *Munsey Trust Co.,* 332 U. S. 234, 242; *Howell* v. *Commissioner,* 69 F. 2d 447 (C. A. 8th), certiorari denied, 292 U. S. 654; *American Sur. Co.* v. *State T. & S. Bk.,* 218 Iowa 1, 254 N. W. 338; *Randell* v. *Fellers,* 218 Iowa 1005; 252 N. W. 787; Brandt, *Suretyship & Guaranty* (3d ed.), Sec. 324; 24 *Am. Jur.,* Sec. 125. Accordingly, while a guarantor by entering into the guaranty contract and making payment thereunder puts himself in a position where he may sustain a loss, it is only if, and to the extent that, the debt which he acquires by subrogation is worthless that he actually sustains a loss. Thus, if the guarantor, having made payment under his guaranty contract, is able to recover in full from the principal debtor, he clearly suffers no loss at all. It follows, therefore, that any loss, the existence and extent of which is wholly and directly dependent

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[13] The guaranty contract was apparently executed and performed in Des Moines, Iowa. (R. 2–4.)

upon the worthlessness of a debt, should be attributed to the worthlessness of that debt, *i. e.*, should be considered a bad debt loss.[14]

Prior to the addition of Section 23 (k) (4) to the Internal Revenue Code of 1939, both the administrative and the judicial construction of the bad debt deduction provisions of the internal revenue laws had long recognized that a guarantor's loss is by its very nature a loss from the worthlessness of a debt. Thus, prior to the enactment of that section in 1942, when, as pointed out *supra* (pp. 14–15), the deduction of nonbusiness bad debt losses was first restricted, numerous administrative rulings and judicial decisions had been issued construing the statutory bad debt deduction provisions as covering guarantors' losses. See, for example, O. D. 556, 2 Cum. Bull. 137 (1920); A. R. R. 479, 5 Cum. Bull. 146 (1921); I. T. 2012, III-1 Cum. Bull. 158 (1924); I. T. 2025, III-1 Cum. Bull. 166 (1924); *Shiman* v. *Commissioner*, 60 F. 2d 65 (C. A. 2d); *Hamlen* v. *Welch*, 116 F. 2d 413 (C. A. 1st); *Gimbel* v. *Commissioner*, 36 B. T. A. 539; *Roberts* v. *Commissioner*, 36 B. T. A. 549; *Sharp* v. *Commissioner*, 38 B. T. A. 166; *Hovey* v. *Commissioner*, decided February 17, 1939 (1939 P-H B. T. A. Memorandum Decisions, par. 39,081); *Pierce* v. *Commis-*

[14] So long as payment of a debt is guaranteed by a solvent guarantor, the insolvency of the principal debtor obviously does not render the debt worthless. Consequently, if the debt which a guarantor acquires by subrogation becomes worthless, it necessarily becomes worthless in the hands of the guarantor rather than in the hands of the original creditor.

sioner, 41 B. T. A. 1261; *Whitcher* v. *Welch,* 22 F. Supp. 763 (Mass.).[15]

Moreover, in the light of this long-standing administrative and judicial construction of the statutory bad debt deduction provisions, Congress repeatedly reenacted those provisions without substantial change and without indicating any disagreement.[16] Nor did Congress indicate any intention to depart from this settled construction when in the Revenue Act of 1942, *supra,* it provided for capital loss treatment of an individual's nonbusiness bad debts. Accordingly, Congress ~~must be~~ deemed, under well-settled principles, to have approved this construction as a correct interpretation

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[15] Similar decisions subsequently rendered include:

Ortiz v. *Commissioner,* 42 B. T. A. 173, reversed on another ground, *sub nom. Helvering* v. *Wilmington Trust Co.,* 124 F. 2d 156 (C. A. 3d), reversed (without discussion on this point), 316 U. S. 164; *Burnett* v. *Commissioner,* decided September 24, 1942 (1942 P-H B. T. A. Memorandum Decisions, par. 42,528); *Ritter* v. *Commissioner,* decided October 9, 1946 (1946 P-H T. C. Memorandum Decisions, par. 46,237); *Greenhouse* v. *Commissioner,* decided August 30, 1954 (1954 P-H T. C. Memorandum Decisions, par. 54,250); *Est. of Rosset* v. *Commissioner,* decided December 30, 1954 (1954 P-H T. C. Memorandum Decisions, par. 54,346); *Watson* v. *Commissioner,* 8 T. C. 569; *Sherman* v. *Commissioner,* 18 T. C. 746; *Aftergood* v. *Commissioner,* 21 T. C. 60; *Stamos* v. *Commissioner,* 22 T. C. 885.

[16] The bad debt deduction provisions of earlier Revenue Acts were enacted in Section 214 (a) (7) of the Revenue Act of 1921, c. 136, 42 Stat. 227; Section 214 (a) (7) of the Revenue Act of 1924, c. 234, 43 Stat. 253; Section 214 (a) (7) of the Revenue Act of 1926, c. 27, 44 Stat. 9; Section 23 (j) of the Revenue Act of 1928, c. 852, 45 Stat. 791; Section 23 (j) of the Revenue Act of 1932, c. 209, 47 Stat. 169, Section 23 (k) of the Revenue Act of 1934, c. 277, 48 Stat. 680, Section 23 (k) of the Revenue Act of 1936, c. 690, 49 Stat. 1648, Section 23 (k) of the Revenue Act of 1938, c. 289, 52 Stat. 447, and Section 23 (k) of the Internal Revenue Code of 1939.

of the statute and to have intended that the bad debt loss provisions would continue to govern a taxpayer's losses as guarantor.[17] *Corn Products Co.* v. *Commissioner,* 350 U. S. 46, 52–53; *Commissioner* v. *Munter,* 331 U. S. 210, 215; *Crane* v. *Commissioner,* 331 U. S. 1, 8; *Commissioner* v. *Flowers,* 326 U. S. 465, 469; *Boehm* v. *Commissioner,* 326 U. S. 287, 291–292; *Douglas* v. *Commissioner,* 322 U. S. 275, 281.

Taxpayer relies chiefly upon recent decisions of some of the Courts of Appeals, disagreeing with those of the Tax Court, to the effect that guarantors' losses are not bad debt losses. See *Cudlip* v. *Commissioner,* 220 F. 2d 565 (C. A. 6th); *Pollak* v. *Commissioner,* 209 F. 2d 57 (C. A. 3d); *Ansley* v. *Commissioner,* 217 F. 2d 252 (C. A. 3d); *Edwards* v. *Allen,* 216 F. 2d 794 (C. A. 5th). As pointed out in the dissenting opinion in the *Cudlip* case, with which the court below agreed (R. 34), the reasoning in those cases will not withstand analysis. It is grounded upon three false assumptions.

First, it is assumed that no distinction should be made between a voluntary and an involuntary acquisition of a worthless debt, and it is accordingly con-

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[17] That Congress has consistently adhered to the treatment of guarantors' losses as bad debt losses is further demonstrated by its subsequent legislation dealing specifically with the deduction of an individual's losses as guarantor of noncorporate obligations. Thus, by Section 166 (f) of the Internal Revenue Code of 1954 (26 U. S. C. 1952 ed., Supp. II, Sec. 166), Congress provided not only that such guarantors' losses may be deducted in full if they meet certain prescribed qualifications but also that they shall be deducted as bad debts. The significance of limiting full deduction to cases involving noncorporate obligations is discussed, *infra*, pp. 29–30.

cluded that the worthless debt which a guarantor involuntarily acquires by subrogation upon being required to make payment under his guaranty contract is no debt at all. This assumption loses sight of the very basis for refusing to treat a voluntary acquisition of a worthless debt as the acquisition of a valid debt. The reason for such treatment is that a trans action in which one voluntarily advances money to another without any expectancy of repayment involves, in reality, no debt at all, but a gratuity. *W. F. Young, Inc.* v. *Commissioner,* 120 F. 2d 159 (C. A. 1st); *American Cigar Co.* v. *Commissioner,* 66 F. 2d 425 (C. A. 2d), certiorari denied, 290 U. S. 699; *Reading Co.* v. *Commissioner,* 132 F. 2d 306 (C. A. 3d), certiorari denied, 318 U. S. 778. No such gratuity is involved in the case of a guarantor whose payment to the creditor is made not voluntarily but because his contractual obligation requires it, and whose loss arises, not because he is making a gift to the primary obligor but because the latter is unable to repay the debt. See 5 Mertens, *Law of Federal Income Taxation* (1953 Rev.), Sec. 30.11, p. 412.

Second, it is assumed (at least in the *Allen* case) that the debt which a guarantor acquires by subrogation does not originate until its acquisition by the guarantor, and it is argued, therefore, that such a debt cannot "become" worthless within the taxable year, within the meaning of Section 23 (k), because it is worthless from its origin. This refined argument misconceives the basis of the doctrine of subrogation, under which payment by a guarantor is treated not

as creating a new debt and extinguishing the original debt owed by the principal debtor to the creditor, but rather as preserving the original debt and merely substituting the guarantor for the creditor. Unless that fundamental concept is repudiated, it is clear that the original debt which a guarantor acquires by subrogation becomes worthless only after he acquires it. The debt certainly was not worthless at its inception, and so long as it remains enforceable against the guarantor, as in this case, it is not worthless to the man who owns it, i. e., the creditor. It becomes worthless only if and when its new owner, i. e., the guarantor, pays the debt and succeeds to the rights of the creditor, and then or thereafter the debt becomes non-collectible against the primary obligor. The fact that a debt may become worthless at the very instant the guarantor acquires it does not negate the existence of the debt.

Third, it is assumed that the nature of the issue presented and the statutory bad debt provisions involved here are the same as in *Eckert* v. *Burnet*, 283 U. S. 140, and that consequently this Court's holding in that case requires a decision in favor of taxpayer here. The issue decided in *Eckert*, however, as this Court later explained in *Helvering* v. *Price*, 309 U. S. 409, related merely to the year in which a taxpayer using the cash method of accounting was entitled to a deduction, either as a bad debt or as a loss not involving a bad debt. The taxpayer there had made no cash payment as guarantor in the taxable year before the Court but had merely substituted his note

on which he was primarily liable for the principal debtor's notes upon which he was secondarily liable. While the Court indicated that the taxpayer might be entitled to a deduction in a later year, when he paid his note, it did not hold that such a deduction would not be a bad debt deduction. Indeed, this Court's only reference in *Eckert* to the statutory bad debt provisions there involved consisted of repeating with approval a statement, which Judge Learned Hand had made in that case in the court below and which he subsequently explained in *Shiman* v. *Commissioner,* 60 F. 2d 65, 66–67 (C. A. 2d), to the effect that, since any debt which Eckert acquired was worthless when he acquired it, there was nothing to charge off. Taxpayer's reliance on that statement is entirely misplaced, since it related to the pre-1942 statutory provision then in effect requiring that a debt in order to be deductible be ascertained to be worthless and charged off within the taxable year (raising a question whether such debt must have been previously carried on the taxpayer's books as a valuable asset), a requirement which, as already pointed out (n. 10, *supra,* pp. 14–15), was subsequently eliminated by the 1942 Act.

Because of the erroneous reasoning upon which the *Cudlip, Pollak,* and like cases relied upon by taxpayer rest, the court below properly declined to follow them. The correct view, we submit, is that expressed in the dissenting opinion in the *Cudlip* case,

approved by the court below. (R. 34.) As Judge Stewart there stated, in part (pp. 570-571):

> As recognized in the majority opinion, it is hornbook law that when a guarantor is compelled to pay the principal creditor, he becomes by operation of law subrogated as a creditor of the principal debtor. In the nature of things, the debt which the guarantor thus acquires is usually worthless at the time of its acquisition. Yet, until the Pollak and Allen cases, and today's decision in this case, the debt so arising has consistently been considered nonetheless deductible as a bad debt, although it became worthless immediately upon its ripening from a secondary obligation into a debt.

The decision of the Second Circuit in *Fox* v. *Commissioner*, 190 F. 2d 101, upon which taxpayer also relies (Br. 13), is inapposite. In issue in that case was a payment which the taxpayer as guarantor was required to make on an indebtedness of her deceased husband, whose estate was insolvent and whose executors had been discharged four years prior to the time such payment was made. Accordingly, when the widow made her payment as guarantor, there was, technically as well as realistically, no principal debtor in existence against whom she could acquire any rights by subrogation. In holding that under those circumstances her loss was not a bad debt loss subject to capital loss limitations, the court, referring to *Pierce* v. *Commissioner*, 41 B. T. A. 1261, and *Gimbel* v. *Commissioner*, 36 B. T. A. 539, stated (p. 105) that its holding did "no violence to the theory that a debt

might arise upon payment by a guarantor where the principal debtor remains still in existence."

In an effort to assimilate the situation here to that presented in *Fox*, taxpayer argues (Br. 12) that the corporation whose debt he guaranteed had disposed of its assets and been liquidated before he made the guaranty payments. The undisputed fact remains, however, that the corporation had not been dissolved but was still in existence at the time. And even if the corporation had been dissolved, it would have remained alive, under the law of Iowa, for the purpose of paying its debts. 28 Iowa Code Annotated § 491.56; *Wisconsin & Arkansas Lumber Co.* v. *Cable*, 159 Iowa 81, 91, 140 N. W. 211. Moreover, where as here the principal debtor is a corporation of which the guarantor is the controlling stockholder, so that the continued existence of the principal debtor is within the control of the guarantor, the tax consequence surely ought not to depend upon whether the guarantor chooses to liquidate and dissolve the insolvent corporation before or after making the guaranty payment.[18]

At any rate, whether or not a guarantor's loss is deductible in full rather than as a capital loss in the exceptional situation presented in the *Fox* case—death of the principal debtor and closing of the administration of his insolvent estate before the guarantor is

[18] Significantly, Section 166 (f) of the Internal Revenue Code of 1954 (quoted in footnote 20, p. 29, *infra*), not only treats a guarantor's payment as a bad debt loss, but authorizes its deduction in full (*i. e.*, as a business rather than a nonbusiness bad debt loss) only where the guaranty is of a noncorporate

called upon to make payment—is a question not here presented and need not here be decided. In the *Fox* case the court had before it an unusual set of facts. However, in the ordinary case, like this one, where the insolvent principal debtor (or its assignee or successor) is in existence when the guaranted payment is made, it is clear that the statute requires the guarantor's loss to be treated as a bad debt loss.

D. *Treatment of the loss as other than a bad debt loss would render the applicability of Section 23 (k) (4) dependent upon the form rather than the substance of the transaction resulting in the loss*

Quite apart from the foregoing, there are important practical considerations which impel the conclusion that Congress intended to treat losses stemming from the guarantee of a corporate debt as bad debt losses subject to the capital loss limitations of Section 23 (k) (4). Congress has provided for capital loss treatment not only of worthless stock losses (Section 23 (g) (2) and (3)), but also of losses resulting from loans to a corporation, whether or not the loan is evidenced by a debt security (Section 23 (k) (2), (3) and (4)). And it made no distinction between lenders and guarantors. There is no real or economic difference—and consequently there should be none for tax purposes[19]—between the loss of an investment made in the form of a direct loan to a corporation and

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[19] Cf. *Higgins* v. *Smith*, 308 U. S. 473; *Griffiths* v. *Commissioner*, 308 U. S. 355; *Gregory* v. *Helvering*, 293 U. S. 465.

one made indirectly in the form of a guaranteed bank loan, especially where as here the guarantor is the dominant stockholder of the corporation.

No valid reason appears, and none is suggested by taxpayer, for imputing to Congress an intent to single out indirect loans, in the form of a guarantee or endorsement of a third party's loan to the corporation, for preferential tax treatment over other types of investments in an unsuccessful corporate enterprise. Even if the legislative intent in this respect were not as plain as it is, "A desire for equality among taxpayers is to be attributed to Congress, rather than the reverse." *Colgate* v. *United States*, 320 U. S. 422, 425. As Judge Stewart pointed out in his dissenting opinion in the *Cudlip* case (p. 572):

> Had the petitioner made the necessary additional investment in the conventional form of subscribing for stock, his loss upon the failure of the corporation would have been a capital loss, § 23 (g) (2), I. R. C. Had he made the investment in the form of a loan to the corporation evidenced by an instrument bearing interest coupons, his loss would likewise have been a capital loss, § 23 (k) (2), I. R. C. Had he made the additional investment in the form of an ordinary loan to the corporation, his loss would likewise have been a capital loss, § 23 (k) (4) I. R. C., Commissioner of Internal Revenue v. Smith, supra.
>
> Because the petitioner happened instead to risk his money by guaranteeing the corporation's bank loans, the court now holds that the petitioner may take an ordinary loss, deductible

in full from his ordinary income. Yet from the petitioner's viewpoint, the situation would have been precisely the same had he himself borrowed the money and then lent it to the corporation. It therefore seems to me that the result reached by the court in this case is significantly unrealistic.

From now on an investor in this Circuit need not be content with a capital loss if he loses his risk capital. If only he can make his investment in the form of a guaranty, his loss will be deductible in full from his ordinary income if the venture is unsuccessful.

The Congressional intent to preclude deduction in full of losses like that here involved, and to treat them as capital losses from nonbusiness bad debts, has been confirmed by and carried over into the Internal Revenue Code of 1954. Section 166 (f) of that Code provides for treatment as a business "bad debt" (*i. e.*, deduction in full) of payments made by a taxpayer as a "guarantor, endorser, or indemnitor," but explicitly confines such treatment to the guaranty of a "noncorporate obligation."[20] Thus Congress in

[20] That section provides:

"A payment by the taxpayer (other than a corporation) in discharge of part or all of his obligation as a guarantor, endorser, or indemnitor of a noncorporate obligation the proceeds of which were used in the trade or business of the borrower shall be treated as a debt becoming worthless within such taxable year for purposes of this section (except that subsection (d) shall not apply), but only if the obligation of the borrower to the person to whom such payment was made was worthless (without regard to such guaranty, endorsement, or indemnity) at the time of such payment."

the 1954 Code not only expressly recognized that losses sustained by guarantors constitute bad debt losses, but made certain that they are subject to capital loss limitations if they result from the guaranty of a corporate debt.

CONCLUSION

For the foregoing reasons, it is respectfully submitted that the judgment of the Court of Appeals is correct and should be affirmed.

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APPENDIX

nternal Revenue Code of 1939:

SEC. 23. DEDUCTIONS FROM GROSS INCOME.

In computing net income there shall be allowed as deductions:

* * * * *

(e) *Losses by Individuals.*—In the case of an individual, losses sustained during the taxable year and not compensated for by insurance or otherwise—

(1) if incurred in trade or business; or

(2) if incurred in any transaction entered into for profit, though not connected with the trade or business; or

(3) of property not connected with the trade or business, if the loss arises from fires, storms, shipwreck, or other casualty, or from theft. No loss shall be allowed as a deduction under this paragraph if at the time of the filing of the return such loss has been claimed as a deduction for estate tax purposes in the estate tax return.

* * * * *

(g) *Capital Losses.*—

(1) *Limitation.*—Losses from sales or exchanges of capital assets shall be allowed only to the extent provided in section 117.

(2) *Securities becoming worthless.*—If any securities (as defined in paragraph (3) of this subsection) become worthless during the taxable year and are capital assets, the loss resulting therefrom shall, for the purposes of this chapter, be considered as a loss from the sale or exchange, on the last day of such taxable year, of capital assets.

(3) [As amended by Sec. 123 (a) (2) of the Revenue Act of 1942, c. 619, 56 Stat. 798] *Definition of securities.*—As used in paragraph (2) of this subsection the term "securities" means (A) shares of stock in a corporation, and (B) rights to subscribe for or to receive such shares.

* * * * *

(k) [As amended by Sec. 124 (a) of the Revenue Act of 1942, *supra*] *Bad Debts.*—

(1) [As amended by Sec. 113 (a) of the Revenue Act of 1943, c. 63, 58 Stat. 21] *General rule.*—Debts which become worthless within the taxable year; or (in the discretion of the Commissioner) a reasonable addition to a reserve for bad debts; and when satisfied that a debt is recoverable only in part, the Commissioner may allow such debt, in an amount not in excess of the part charged off within the taxable year, as a deduction. This paragraph shall not apply in the case of a taxpayer, other than a bank, as defined in section 104, with respect to a debt evidenced by a security as defined in paragraph (3) of this subsection. This paragraph shall not apply in the case of a taxpayer, other than a corporation, with respect to a nonbusiness debt, as defined in paragraph (4) of this subsection.

(2) *Securities becoming worthless.*—If any securities (as defined in paragraph (3) of this subsection) become worthless within the taxable year and are capital assets, the loss resulting therefrom shall, in the case of a taxpayer other than a bank, as defined in section 104, for the purposes of this chapter, be considered as a loss from the sale or exchange, on the last day of such taxable year, of capital assets.

(3) *Definition of securities.*—As used in paragraphs (1), (2), and (4) of this subsection the term "securities" means bonds, debentures, notes, or certificates, or other evidences of indebtedness, issued by any corporation (including those issued by a government or political subdivision thereof), with interest coupons or in registered form.

(4) *Non-business debts.*—In the case of a taxpayer, other than a corporation, if a non-business debt becomes worthless within the taxable year, the loss resulting therefrom shall be considered a loss from the sale or exchange, during the taxable year, of a capital asset held for not more than 6 months. The term "non-business debt" means a debt other than a debt evidenced by a security as defined in paragraph (3) and other than a debt the loss from the worthlessness of which is incurred in the taxpayer's trade or business.

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(26 U. S. C. 1952 ed., Sec. 23.)

SEC. 117. CAPITAL GAINS AND LOSSES.

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(d) [As amended by Sec. 150 (c) of the Revenue Act of 1942, supra] *Limitation on Capital Losses.*—

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(2) *Other taxpayers.*—In the case of a taxpayer, other than a corporation, losses from sales or exchanges of capital assets shall be allowed only to the extent of the gains from such sales or exchanges, plus the net income of the taxpayer of [or] [sic] $1,000, whichever is smaller. * * *

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(26 U. S. C. 1952 ed., Sec. 117.)

Treasury Regulations 111, promulgated under the Internal Revenue Code of 1939:

SEC. 29.23 (e)-1. *Losses by Individuals.*—Losses sustained by individual citizens or residents of the United States and not compensated for by insurance or otherwise are fully deductible if (a) incurred in the taxpayer's trade or business, or (b) incurred in any transaction entered into for profit, or (c) arising from fires, storms, shipwreck, or other casualty, or theft, and a deduction therefor has not prior to the filing of the return been claimed for estate tax purposes in the estate tax return, or (d) if not prohibited or limited by any of the following sections of the Internal Revenue Code: Sections 23 (g) and 117, relating to capital losses; section 23 (h), relating to wagering losses; section 24 (b), relating to losses from sales or exchanges of property between persons designated therein; section 112, relating to recognition of gain or loss upon sales or exchanges of property; section 118 relating to losses on wash sales of stock or securities; section 251, relating to income from sources within possessions of the United States; and section 252, relating to citizens of possessions of the United States. See section 213 as to limitation upon losses sustained by nonresident aliens.

In general losses for which an amount may be deducted from gross income must be evidenced by closed and completed transactions, fixed by identifiable events, bona fide and actually sustained during the taxable period for which allowed. Substance and not mere form will govern in determining deductible losses. Full consideration must be given to any salvage value and to any insurance or other compensation received in determining the amount of losses actually sustained. See section 113 (b).

For special provisions with respect to war losses, see section 127.

*   *   *   *   *

A loss on the sale of residential property purchased or constructed by the taxpayer for use as his personal residence and so used by him up to the time of the sale is not deductible. If, however, property so purchased or constructed is prior to its sale rented or otherwise appropriated to income-producing purposes and is used for such purposes up to the time of its sale, a loss from the sale of the property, computed as provided in section 111, is, subject to the limitations provided in section 117, an allowable deduction in an amount not to exceed the excess of the value of the property at the time it was appropriated to income-producing purposes (with proper adjustment for depreciation) over the amount realized from the sale.

*   *   *   *   *

Sec. 29.23 (g)–1. *Capital Losses.*—Section 23 (g) provides in effect that deductions allowed to individuals under section 23 (e) and to corporations under section 23 (f) for losses sustained on the sale or exchange of a capital asset shall be limited in amount to the extent provided in section 117. * * *

*   *   *   *   *

Sec. 29.23 (k)–6 [As amended by T. D. 5458, 1945–1 Cum. Bull. 45]. *Non-business Bad Debts.*—In the case of a taxpayer, other than a corporation, if a non-business bad debt becomes entirely worthless within a taxable year beginning after December 31, 1942, the loss resulting therefrom shall be treated as a loss from the sale or exchange of a capital asset held for not more than six months. Such a loss is subject to the limitations provided in section 117 with respect to gains and losses from the sale and exchange of capital assets. A loss with respect to such a debt will be

treated as sustained only if and when the debt has become totally worthless, and no deduction shall be allowed for a non-business debt which is recoverable in part during the taxable year. Nor are the provisions of this subdivision applicable in the case of a loss resulting from a security as defined in section 23 (k) (3). A non-business debt is a debt other than a debt the loss from the worthlessness of which is incurred in the taxpayer's trade or business and other than a debt evidenced by a security as that term is defined in section 23 (k) (3). The question whether a debt is one the loss from the worthlessness of which is incurred in the taxpayer's trade or business is a question of fact in each particular case. The determination of this question is substantially the same as that which is made for the purpose of ascertaining whether a loss from the type of transaction covered by section 23 (e) is "incurred in trade or business" under paragraph (1) of that section.

The character of the debt for this purpose is not controlled by the circumstances attending its creation or its subsequent acquisition by the taxpayer or by the use to which the borrowed funds are put by the recipient, but is to be determined rather by the relation which the loss resulting from the debt's becoming worthless bears to the trade or business of the taxpayer. If that relation is a proximate one in the conduct of the trade or business in which the taxpayer is engaged at the time the debt becomes worthless, the debt is not a non-business debt for the purposes of this section.

* * * * *